

[COMMITTEE PRINT]

REPORT  
OF THE  
*U.S. Post Office Dept.*  
ADVISORY PANEL ON POSTAL RATES

PREPARED BY THE  
POST OFFICE DEPARTMENT  
FOR USE OF THE  
COMMITTEE ON POST OFFICE AND  
CIVIL SERVICE  
HOUSE OF REPRESENTATIVES



MAY 1965



U.S. GOVERNMENT PRINTING OFFICE

48-160

WASHINGTON : 1965

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1965

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## FOREWORD

This committee print contains (1) a letter from Assistant Postmaster General Ralph W. Nicholson, transmitting a copy of the report of the Advisory Panel on Postal Rates, (2) a letter of transmittal from the Advisory Panel to the Postmaster General, and (3) the report of the Advisory Panel.

The seven-member Advisory Panel on Postal Rates was appointed by the Postmaster General on January 22, 1965, to assist him in developing policy on postal rates. The Advisory Panel's report was transmitted to the Postmaster General on May 3, 1965. Members of the Panel were:

Hon. Robert Ramspeck, Chairman, former Congressman and former Chairman of the U.S. Civil Service Commission.

Walker Lee Cisler, Grosse Point Park, Mich., president, Detroit Edison Co.

Robert H. Rawson, Shaker Heights, Ohio, vice president and general manager, Empire Plow Co.

John W. Snyder, Toledo, Ohio, president, Overland Corp., and former Secretary of the Treasury.

Dr. Robert C. Turner, Bloomington, Ind., professor of business economics and public policy, University of Indiana.

Mrs. Mary Roebling, Trenton, N.J., chairman of the board, Trenton Trust Co.

James A. Suffridge, Arlington, Va., president, Retail Clerks International Association.

The Panel's recommendations to the Postmaster General were summarized as follows:

1. Seek legislation to discontinue all preferential rates which now account for nearly \$300 million of tax-supported public service costs. If subsidies are justified, they should be paid directly from Treasury funds rather than indirectly via postal rates.

2. Pay the cost of rural facilities in full from postal revenues. No part of these costs should be considered a subsidy for payment from general funds of the Treasury.

3. Continue the cost ascertainment system, apportioning costs on a fully allocated basis.

4. Seek additional rate guidelines that would be more complete than those which now appear in the Postal Policy Act.

5. Formulate plans for a general rate increase.

6. Include the following concepts in rate increase plans: (1) A merger of surface and air letter mail into a single service, accompanied by a policy that the fastest available transportation will be furnished; (2) a change in second-class rates giving greater emphasis to basic piece handling charges for each copy.

7. Revise the Department's mail classification system.

TOM MURRAY,

*Chairman, Committee on Post Office and Civil Service.*

**LETTER OF TRANSMITTAL**

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POST OFFICE DEPARTMENT,  
ASSISTANT POSTMASTER GENERAL,  
BUREAU OF FINANCE AND ADMINISTRATION,  
*Washington, D.C., May 21, 1965.*

HON. TOM MURRAY,  
*Chairman, Committee on Post Office and Civil Service,  
House of Representatives, Washington, D.C.*

DEAR MR. CHAIRMAN: I am attaching a copy of the report to the Postmaster General by the Advisory Panel on Postal Rates. It was handed to the press this morning for release at 6:30 p.m. today.

Sincerely yours,

RALPH W. NICHOLSON,  
*Assistant Postmaster General.*

▼

## LETTER OF SUBMITTAL

ADVISORY PANEL ON POSTAL RATES,  
Washington, D.C., May 3, 1965.

HON. JOHN A. GRONOUSKI,  
Postmaster General,  
Washington, D.C.

DEAR MR. GRONOUSKI: We transmit herewith the report of your Advisory Panel on Postal Rates. It is in compliance with your request to review postal rate policy.

Panel members discussed the problem with numerous individuals and groups so as to get the views of the general public. Your headquarters provided technical guidance and information in the form of reports and briefings. Postmasters responded generously to our request for help and we benefited greatly from conducted tours of postal operations. In addition, we sought the views of some 60 organizations representing major mail users and postal employees. Replies from 47 companies and organizations furnished a cross section of opinions.

We would not presume to say our work has developed a full understanding of every aspect of postal operations. Of necessity, the Panel focused its study on those facets of the service that have a direct bearing on postal rates.

Our report reflects views and judgments that are entirely our own, sometimes in accord with but often at variance from the views of mail users and your technical staff. We hope they will stimulate discussion and lead to basic changes in rate policy and rate practices. Three months of intensive study and long hours at the conference table have convinced us there is need for change.

We express our gratitude for the opportunity to be of service.

Respectfully,

ROBERT RAMSPECK,  
*Chairman.*

WALKER CISLER.  
ROBERT H. RAWSON.  
MARY ROEBLING.  
JOHN W. SNYDER.  
JAMES A. SUFFRIDGE.<sup>1</sup>  
R. C. TURNER.

<sup>1</sup> I hereby concur in the committee report except for the portion dealing with the abolition of special rate publications published by nonprofit associations; such as, churches, labor unions, etc., which I oppose.

J.A.S.

VII

## REPORT OF THE ADVISORY PANEL ON POSTAL RATES

The Post Office Department must now draw heavily on tax revenues to augment postal revenues. Receipts from mail users are estimated this year to fall short of covering the Department's costs by about \$762 million, an amount that must be made up from general funds of the Treasury.

This Panel believes that postal costs as a whole should be met from postal receipts and reimbursements for services to other Government organizations. We see no basic conflict between the performance of public service and the requirement that mail users should pay for whatever service they receive. First-class mail is a public service. Its service and value to the Nation are far greater than in any other class of mail. Yet few would contend that users of first-class mail should not pay the full cost of the service they receive.

The actions proposed by this Panel are mainly along two lines: (1) revising the Postal Policy Act, and (2) raising postal rates, with particular emphasis on preferential rates that are now identified as public service subsidies.

The findings underlying the Panel's recommendation are outlined below. The recommendations are these:

1. Seek legislation to discontinue all preferential rates which now account for nearly \$300 million of tax-supported public service costs. If subsidies are justified, they should be paid directly from Treasury funds rather than indirectly via postal rates.
2. Pay the cost of rural facilities in full from postal revenues. No part of these costs should be considered a subsidy for payment from general funds of the Treasury.
3. Continue the cost ascertainment system, apportioning costs on a fully allocated basis.
4. Seek additional rate guidelines that would be more complete than those which now appear in the Postal Policy Act.
5. Formulate plans for a general rate increase.
6. Include the following concepts in rate increase plans:  
(1) A merger of surface and air letter mail into a single service, accompanied by a policy that the fastest available transportation will be furnished; (2) a change in second-class rates giving greater emphasis to basic piece handling charges for each copy.
7. Revise the Department's mail classification system.

### RATE POLICY

Under present policies, the Post Office has two tightly interwoven tasks: it must deliver the mail and, through the rate structure, it must play a major role in fulfilling public service objectives.

The Postal Policy Act states, in part:

1. The post office is a public service.
2. It is not a business enterprise conducted for profit or for raising general funds.

To promote compliance with these standards, the Postal Policy Act, as amended, furnishes these rate guidelines:

1. First-class mail is a "preferred" service and postage must cover allocated expenses plus "an additional amount representing the fair value of all extraordinary and preferential services, facilities, and factors relating thereto."

2. Postal rates shall be adjusted so that revenues approximately equal cost, less the total loss incurred for an identified list of public services. For preferential-rate mails, "total loss" is defined as the amount by which fully allocated costs exceed postage.

Supplementing the rate guidelines of the Postal Policy Act, the postal laws require a break-even operation, within 4 percent, for zone-rate fourth-class mail (parcel post and catalogs).

This Advisory Panel is concerned about the precipitous rise in tax-supported public service costs. They have increased from about \$37 million in 1960 to nearly \$500 million now. Some of the increase was a direct result of the rapid growth of preferred-rate mail, particularly in the nonprofit categories and in fourth-class educational materials. Other increases resulted from changes in statute enacted by the Congress: the list of public service items was expanded and a "total loss" formula was substituted for "revenue forgone" as the measure of public service costs on reduced-rate mails.<sup>1</sup>

The Panel believes that all postal costs should be paid from postal revenues and reimbursements for services to other Government agencies. Congress has the right to extend subsidies as a matter of national policy. However, we question whether these subsidies should be intermingled with postal rates. If there is merit in these subsidies, they should be identified and included as direct payments from the budgets of the Federal agencies charged with overseeing public welfare activities. Since rate policy and subsidies are now commingled, the Postmaster General is in a position that compels him to propose rates based on extraordinary welfare considerations as well as on conventional value-of-service and cost criteria.

Responsibility for subsidies to airlines was removed from the Post Office in 1953 and transferred to the Civil Aeronautics Board. Also, responsibility for mail subsidies to steamship lines was shifted from the Post Office to the Maritime Commission, following enactment of the Merchant Marine Act, 1936. Similar changes should be made for all postal subsidies that stem from preferential rates. These now give rise to about \$300 million of public service costs yearly.

The Panel is concerned that public service subsidies are incurred on behalf of nonprofit organizations, publishers, and other mailers without adequate review by the Congress or by executive agencies.

There are few provisions to insure that public service costs on reduced-rate mails do, indeed, serve the public interest. In the judgment of this Panel, many mailings of reduced-rate publications, phonograph records, circulars, and merchandise do not serve any special public interest that would justify tax-supported subsidies. Substantial rate reductions are available to many organizations, for unlimited quantities of mail, on the grounds that the Internal Revenue Service has ruled they are entitled to tax-exemption status. We believe these subsidies should be reexamined by the Congress and only

<sup>1</sup> "Revenue forgone" is the amount of rate concession from the regular rates paid by general users of the mail. "Total loss" is the difference between actual receipts from reduced-rate mails and their fully allocated costs.

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where there is a specific finding of public interest should they be permitted. Such subsidies could take the form of rebates to mail users of a portion of their total postage costs. Moreover, funds for subsidies should be provided by direct appropriation, to the agency overseeing the welfare activity, rather than as a hidden cost in the postal budget.

Ideally, subsidies to preferred mail users should follow the practice in the airline and maritime industries. Issuance of a license or permit by the agency directly charged with supervision of those industries is a precondition for payment of subsidy.

Another segment of public services, about \$97 million yearly, results from costs associated with rural facilities: third-class post offices, the star route system, fourth-class post offices, and rural routes. This Panel does not subscribe to the policy which identifies these expenses as public service costs, paid from taxes rather than from postage. Rural service is essential in a national transportation network and without it much of the urban mail volume would not materialize. The Post Office Department reports that nearly 10 million families—over 35 million persons—are served by rural routes. In addition to their deliveries by these routes, third- and fourth-class offices deliver about 3 billion pieces of mail yearly.

Where costs of rural facilities can be reduced by furnishing equivalent or better service by some other means, that action should be taken.

Recommendation

The Postmaster General should seek legislation to discontinue all preferential rates which now account for nearly \$300 million of tax-supported public service costs. If subsidies are justified, they should be paid directly from Treasury funds rather than indirectly via postal rates.

Recommendation

The cost of rural facilities should be met in full from postal revenues and no part of these costs should be considered a subsidy for payment from general funds of the Treasury.

POSTAL FINANCES

The latest data supplied by the Post Office Department are for the fiscal year 1964, adjusted for the full effect of known higher rates and costs. Postal revenues and reimbursement fall about \$780 million short of costs. Costs are \$5,151 million, so there is a 15-percent deficiency, requiring Treasury financing.

The "total loss" on public services, identified by statute, amounts to \$481 million on a current annual basis. Subtracting that amount from total Treasury financing, according to the provisions of the Postal Policy Act, as amended, the deficit for ratemaking purposes is \$299 million.

These are the key financial data for the service as a whole. A more complete presentation would require a report on the status of revenues and costs for at least the principal mail services. But we must acknowledge that to do so requires entry into an area of disputed data: the products of the Department's cost ascertainment system. We reviewed the system and the contentions of mail users who filed mem-



memorandums in response to our invitation. Our observations and reactions are outlined below.

#### THE COST ASCERTAINMENT SYSTEM

The cost ascertainment system is required by law. Costs are apportioned to each class of mail based on sample observations of actual use of manpower, transportation space, facilities, and equipment. In addition, each mail service is assigned a pro rata share of overhead costs, roughly in proportion to the more direct costs of each service.

It is the contention of the Department's technical staff that judgments of intangible values—such as the priority accorded first class—should not affect cost allocations. In fact, they assert, by definition "intangibles" cannot be expressed in measurable costs.

Many mailers have long advocated an out-of-pocket or incremental cost approach instead of fully allocated costs. The proponents of that approach contend the Post Office Department exists primarily for first-class mail and therefore many of the postal service costs exist for this reason alone.

Not all criticisms of the cost ascertainment system relate to the dispute over incremental versus fully allocated costs. There are criticisms of methods as well, within the framework of the present cost ascertainment approach.

The Advisory Panel spent much time reviewing cost ascertainment methods and examining arguments for and against the system. While some members believed that changes in methods could be made, all agreed that such changes would not significantly affect the level of cost allocations or cost coverage relationships for any classes of mail. Moreover, we were advised the Department is now in the second year of a major effort to improve the cost ascertainment system through more scientific sampling approaches.

On the issue of basic cost approach—fully allocated versus incremental costs—it is the Panel's considered opinion that controversy has clouded reason. Postal rates have never been equated with fully allocated costs. Even if costs were reworked on an incremental basis there would still be wide disparities between such costs and rates.

The essential point is that neither fully allocated nor incremental costs can be an easy path to rates. In either case judgments must enter the ratemaking process.

While we can understand and sympathize with any embarrassment second- and third-class users may suffer because of low cost coverage figures, there is no evidence that such figures have impelled the Congress to approve excessively high rates.

We advise the Postmaster General to continue apportioning costs on a fully allocated basis. Also we believe that the cost accounting process should not be blurred by intangible values. The ratemaking process, not the cost finding process, is the proper place to allow for these intangible values. In giving that advice we are gratified to find that the weight of independent opinion supports our own judgment.

#### *Recommendation*

The Department should continue its cost ascertainment system, apportioning costs on a fully allocated basis.

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## THE NEED FOR RATE GUIDELINES

This Advisory Panel does not believe the longstanding controversy over cost allocations will be dispelled easily. This is regretted, for we are concerned that dispute over cost allocations has needlessly blurred more important issues.

Whichever cost distribution system is followed, the Department and the Congress cannot be relieved of value judgments. If neither fully allocated nor incremental costs were available to indicate cost-revenue relationships for classes of mail and services, the ratemaking process would not come to a halt.

Cost-revenue relationships have not been the dominant influences in the legislative ratemaking process. Service preferences, mail value, availability of alternative services, the interests of users, and broad socioeconomic objectives have been the principal considerations in determining rates.

The cost ascertainment system supplies much valuable data, not only for rate purposes but for the budgetary process, for mail counts, for workload projections, and for many other essential management purposes. The system should be continued. However, we believe the Department, the Congress, and the users of the mail would benefit greatly if cost allocation data were augmented by value-of-service standards for ratemaking. The function of these standards would be to insure equitable interclass relationships and compliance with such cost coverage requirements as the Congress may set for the postal service as a whole.

While the Postal Policy Act expresses the will of Congress in respect to the total financial posture of the postal service, it offers no specific guidance on rates except to state that first-class postage must be in excess of allocated expenses. (Elsewhere, the postal laws also call for a break-even position, within 4 percent, in the fourth-class parcel post-catalog service.) Significantly, while controversies over legislative rate adjustments have centered mainly around second and third class, the Postal Policy Act offers no guidelines for setting their rates. Thus, in the absence of more complete guidelines, rate deliberations must traverse the same difficult ground whenever there is any large imbalance between postal costs and revenues.

The void in the Postal Policy Act could be filled if the Congress would evaluate the different classes of mail on the basis of their service values and other intangibles. The latter would include the social, economic, and cultural importance of each mail class. These evaluations could be expressed in cost coverage percentages. Alternatively, the Congress could supply value-of-service guidelines by stating how rates for the various classes should be scaled in relation to each other. This has long been accepted practice for international mail rates which follow a chart of relationships that has appeared in every Universal Postal Union Convention since 1874. A "relativity" principle requires most rates to be set at specified percentages of the basic rate for letters. That principle could be employed to arrive at an equitable system of minimum rates or piece charges for the principal classes of mail in the domestic postal service. Beyond minimum levels, rates could be scaled upward to compensate for added mail weights or for distant hauls when transportation is a significant cost element.

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In all but first class, mail users frequently assert that rate schedules should recognize deferred service. We believe their point is valid. However, we noted that in many instances "deferred service" is a fiction. In second class, for example, many newspapers and weekly magazines are delivered with greater dispatch than first-class mail. This Panel holds the opinion that, when the Congress enacts less-than-costs rates in recognition of deferred service, the law should also authorize deferment as a standard precondition for such rates.

#### *Recommendation*

The Postmaster General should seek additional rate guidelines that would be more complete than those which now appear in the Postal Policy Act. Expanded guidelines should reflect the judgement of the Congress on the weight to be assigned to value of service and socioeconomic considerations, in setting rates for each major category of mail. Rate guidelines should be stated as approximate cost coverage levels; as rate relationships similar to those employed in the Universal Postal Union Convention; or as a combination of both

#### MEETING THE POSTAL DEFICIENCY

The Department's estimated revenue deficiency for 1965, as reported by the Postmaster General to the Congress, is about \$762 million. The question then is how to finance this deficit. We do not ask whether it should be financed for, indeed, all costs will be paid through postage, taxes, or a combination of both.

As a first step, we believe the Department and its patrons have a joint obligation to pare postal costs. We are gratified that both have recognized that obligation. Much progress has been made by their joint efforts and even more promising gains are expected from programs that are nearing fruition. But even if the Department's most optimistic hopes are realized, cost reductions would still fall several hundred million dollars short of closing the Department's revenue gap.

It would be unrealistic to conclude that cost changes will move in only one direction. Even now there is a possibility of salary increases to reflect the comparability principle enunciated by the Congress in 1962. As this Panel judges these crosscurrents in the cost situation, the Department would do well if its cost cutting and modernization programs are productive enough to offset other cost increases.

There is an urgent need for rate increases and the size of the deficit suggests that few, if any, categories of mail should be exempt from rate increases.

The Post Office Department has embarked on a major cost-cutting, modernization program that is partly dependent on the cooperation of all patrons. For many business and institutional mailers, the required cooperative efforts will have the same effect on their costs as rate increases. And since the Department will determine the scheduling of cooperative programs, it will also decide when mailers will absorb the attendant cost increases. Consequently, while we believe that rate increases should not be delayed for long, the Postmaster General must exercise careful judgment in proposing how they should be phased.

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On specific rate approaches, the Panel endorses the view that surface first-class mail and airmail should be merged into a single service, with transportation by the fastest available means. This change must take place if we hope to see the mail service conform with the shifting patterns in transportation capacity. Also, unless that change is made, mail deliveries will not share the faster service our Nation has come to expect from its vast transportation network.

If first-class and airmail are merged, we believe a higher rate than the present first-class rate should be charged. We suggest consideration of two rates: one rate for standard service and a higher rate where the mailer requests priority handling within post offices.

In second-class mail, the Panel believes that rates should be redesigned, establishing an adequate piece charge that reflects the realities of second-class costs. If this were done, all publications would be subject to a basic handling and delivery charge. Postage in excess of that charge, for each copy mailed, should be scaled in relation to line-haul transportation costs.

#### *Recommendation*

The Department should formulate plans for a general rate increase.

#### *Recommendation*

Rate increase plans should include the following concepts: (1) A merger of surface and air letter mail into a single service, accompanied by a policy that the fastest available transportation will be furnished; (2) a change in second-class rates giving greater emphasis to basic piece handling charges for each copy.

#### MAIL CLASSIFICATION

This report would not be complete without comment on another aspect of the postal service that is closely related to rates: The law defines four major classes of mail. But these have been splintered into a score or more subclasses. The postal classification system is no longer a logical grouping of mails. It is a patchwork of subclasses, each subject to a different rate.

Because of the way the four classes were splintered, there is a wide assortment of inconsistent principles and rules. Some of the classes and subclasses are defined by the physical characteristics of their mails. The definition of other classes includes a requirement for preparation by the mailer. Quite often, classes are determined by the contents of the mail, irrespective of their physical characteristics or the processing required. In other cases, subclasses are defined by the economic and social function of the mailer, or in some instances by that of the recipient.

The chief merit of the system, and apparently the main reason for its present design, is that it is an expedient means of extending rate concessions in the least obtrusive manner. This has led to suggestions that the need is not for four classes, but for as many classes as there are different rates. In effect, each subclass would become a separate mail class. The thought behind that suggestion is that it would lift much of the mystery that now envelops the classification structure. Also, the service and cost-revenue features of each new class could be scrutinized more readily by the public and the Congress.

While a complete overhaul of the postal classification system is needed, the fact is the present system reflects numerous political and economic realities. Many businesses and institutions have been built and nurtured with sustenance from rate concessions. Change would have to allow a reasonable adjustment period in order to prevent hardship. Rates and classifications are entwined so that one cannot be altered without affecting the other. Nevertheless, some long-range planning should be started on mail classifications. One of the key concepts that should be explored concerns the use of rate incentives to achieve desirable operating and cost objectives. Underlying that concept is the conviction that postal modernization has two complementary parts: the steps that mailers can take and the innovations within the Postal Establishment.

A key objective of reclassification should be the harnessing of business and institutional capacities, putting them to work to simplify postal operations and to improve postal productivity. Incentive rates and improved mail classifications could serve as inducements for large mailers to extend their premailing preparation: sorting, bagging, palletizing, transporting, etc. The payoff in reduced operating costs and lower capital outlays for the postal service would make a significant contribution toward meeting the current revenue deficiency. Also, incentive rates may enable volume mailers to cut their own mail costs.

#### *Recommendation*

The Department's mail classification system should be revised. The present numerous rate categories and subclasses should be set apart with separate and clearly defined classification criteria for each. Planning for a revision of the mail classification system should begin at once.

